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More Tough Times Ahead For Car Dealerships

Stingy credit and a shortage of used cars will put a double whammy on dealers.

By Jim Ostroff, Associate Editor, ***The Kiplinger Letter***
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For automakers, 2010 should bring some stability, with total U.S. sales of about 12 million vehicles and most carmakers turning the corner to profitability.

New-car dealers, however, will go through another rough year. Lenders' tightfistedness will make it tough for businesses and consumers to spring for a new set of wheels, despite vehicle prices being about the same as last year's.

Toyota dealers are in for an especially tough time in light of the safety recall and halt in sales of vehicles that account for roughly two-thirds of Toyota's U.S. sales. Dealers' earnings will be depressed for several months.

Meanwhile, lenders are likely to pressure dealers to step up payments on loans for cars sitting on lots for 90 days or more. That will weaken dealers' cash reserves, increasing the odds they'll run out of cash and have little choice but to close shop. Some may try to sell out to another dealer but that's a "very tough sell in this market," says **John Pico, managing partner with Advising Automobile Dealers, a dealer consultancy**.

Dealers selling used cars -- usually a profit mainstay -- face their own woes. Securing supplies of late model vehicles will prove unusually tough, requiring dealers to sweeten deals on trade-ins. Used car prices are likely to climb 5% again this year.

Uncle Sam's Cash for Clunkers program last year helped dry up supplies, even though the 750,000 cars sent to the scrap heap were mainly older cars, sport utility vehicles and pickup trucks. Moreover, rental car companies, which usually send tens of thousands of vehicles to dealers and automobile auction houses, are keeping vehicles longer, reducing supplies.

The slowly rebounding economy and persistently high unemployment rate are boosting demand for used vehicles, too. "For many consumers, the only way to buy a vehicle is to get a used one, since the amount they need to finance is less than (with) new ones, and generally the APR (annual percentage rate) interest rates are a bit lower, too," says Tom Webb, chief economist with Manheim Consulting, a used vehicle consultancy.